Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98

COMMENTS

National Exchange Carrier Association, Inc.
100 South Jefferson Road
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May 16, 1996

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SUMMARY

With this proceeding, the Commission implements the provisions of the Telecommunications Act of 1996 which require interconnection to open the local telecommunications markets to competition. Section 251 of the Act sets forth the local interconnection obligations of all telecommunications carriers, including specific obligations for local exchange carriers ("LECs") and incumbent LECs. These are the obligations upon which, under section 252, any negotiations, agreements, or arbitration will be based, and upon which prices will be determined.

NECA urges the Commission to carefully coordinate the outcome of this proceeding with the existing universal service and potential access reform proceedings to avoid rule conflicts and confusion in the industry. More specifically, this proceeding should not adversely impact upon the Commission's interstate access charge system or universal service principles.

The local interconnection provisions being implemented in this proceeding do not apply to interstate access or the provision of interexchange service. The 1996 Act does not provide any legal basis for permitting IXCs to avoid existing interstate access charge rules. Thus, rules or policies promulgated in this proceeding should recognize that current jurisdictional separations remain and that any changes to these procedures must be made via the Joint Board process.

In promulgating any local interconnection pricing guidelines, the Commission should avoid specifying detailed rate structures, particularly where those rate structures would conflict with existing access charge rules. Instead, broader more flexible rules would allow telephone companies to recognize the differences in serving different classes of customers, different geographical areas, different density areas, individual customer requirements, and differences in underlying technology. Such broad guidelines would support the use of negotiations as contemplated in the Act.

LECs should be permitted to fully recover their embedded costs which were incurred under their obligation as carriers of last resort. Long run incremental cost (LRIC) and total service LRIC (TSLRIC) are not useful methodologies for this purpose. Nothing in the 1996 Act precludes cost-based regulation that would allow for recovery of embedded costs for determining the prices and rate structure of local interconnection. The Commission should also include a transition period or other cost-recovery mechanism in implementing any such new rules.

The Commission should also carefully consider the effects of its rules on rural incumbent LECs. Interconnection rules developed with the larger companies in mind, but applied "across the board," can have unintentional, negative impacts on smaller rural companies with different cost and service structures, and minimal or no competition.

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COMMENTS

The National Exchange Carrier Association, Inc. (NECA)[1] submits its comments in response to the Commission's Notice of Proposed Rulemaking (NPRM) in the above-captioned matter.[2]

I. INTRODUCTION

New section 251 of the Communications Act sets forth the local interconnection obligations of all telecommunications carriers, including specific obligations for local exchange carriers ("LECs") and incumbent LECs. These are the obligations upon which, under section 252, any negotiations, agreements, or arbitration will be based, and upon which prices will be determined.[3]

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[1] NECA is a not-for-profit association that is responsible, under the Commission's rules, for the preparation of access charge tariffs on behalf of over 1,200 telephone companies that do not file separate tariffs; and for the collection and distribution of access charge revenues. *See* 47 C.F.R. §§ 69.603 and 64.604. NECA also administers the interstate Universal Service and Lifeline Assistance programs and the interstate Telecommunications Relay Services (TRS) fund. *See id.*

[2] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, *Notice of Proposed Rulemaking*, FCC 96-182 (rel. April 19, 1996) (*NPRM*). The *NPRM* seeks comment on various approaches to implement the local competition provisions, including sections 251 and 252, contained in the Telecommunications Act of 1996, Pub. L. 104-104, 110 Stat. 56 (1996) (to be codified at 47 U.S.C. §§ 151 *et. seq.*) (the "1996 Act"). Issues to be addressed include: the interconnection obligations of local exchange carriers; pricing standards pursuant to those obligations; and negotiation, arbitration and agreement procedures.

[3] Under section 252(d), charges for interconnection and for network elements are to be determined based on cost; charges for transport and termination of traffic are to be based on

As the Commission notes, the purpose of this proceeding is to implement the provisions of the 1996 Act which require interconnection to open the *local* telecommunications markets to competition.[4] Nevertheless, the Commission recognizes an interrelationship between this proceeding, its universal service proceeding, and its "upcoming proceeding to reform our Part 69 access charge rules," and asks commenters to bear this interrelationship in mind as they frame their proposals.[5]

While this NPRM addresses local interconnection, guidelines or rules that implement such interconnection may indirectly impact the access charge system since many of the same facilities are used to provide both local and interstate access services. As administrator of access charge tariffs for over 1,200 incumbent LECs, NECA asserts in its comments that this proceeding must not adversely impact upon the Commission's interstate access charge system. NECA urges the Commission to carefully coordinate the outcome of this proceeding with the existing Universal Service[6] and potential access reform proceedings to avoid policy conflicts, industry confusion, and numerous clarification and complaint filings.

NECA's comments address the following key points: (1) sections 251 and 252 do not apply to interstate access or the provision of interexchange service, and rules or policies promulgated in this proceeding must recognize that current jurisdictional separations remain; (2) any local interconnection

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reciprocal compensation; and wholesale rates for resold telecommunications services are to be determined by the State commissions based on retail rates minus "avoided costs." Telecommunications Act of 1996, H.R. Report 104-458, *Joint Explanatory Statement* at 125-126 (*Joint Explanatory Statement*).

[4] *NPRM* at ¶¶ 1- 2.

[5] *Id.* at ¶ 3.

[6] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Notice of Proposed Rulemaking and Order Establishing Joint Board*, 61 Fed. Reg. 10499 (March 14, 1996) (*USF NPRM*).

pricing guidelines promulgated should not specify detailed rate structures, particularly where those rate structures would conflict with existing access charge rules; (3) LECs, especially rural incumbent LECs, should be permitted to fully recover their embedded costs which were incurred under their obligation as carriers of last resort; and (4) the Commission should carefully consider the effects of its rules on rural incumbent LECs.

II. SECTIONS 251 AND 252 DO NOT APPLY TO INTERSTATE ACCESS[7]

In the NPRM, the Commission directly addresses the question of whether IXCs can avoid interstate access charges through the 1996 Act's local interconnection provisions.[8] Sections 251 and 252 do *not* apply to IXCs for purposes of providing originating and terminating interexchange services. As discussed below, the 1996 Act's local interconnection provisions do not provide any legal basis for permitting IXCs to avoid interstate access charges.

First, the Commission cannot ignore the separations rules for allocating joint costs between the interstate and intrastate jurisdiction that are currently in place and cannot change these rules without a recommended decision of a Joint Board.[9] Because these separation rules remain valid, the 1996 Act's local interconnection arrangements may address only the recovery of intrastate costs. Therefore, the Commission must continue to allow recovery of jurisdictionally assigned interstate costs under the Part 69 access charge structure. The Commission may decide to adapt its Part 69

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[7] Addressing primarily section II. B. 2. e. of the NPRM, "Interexchange Services," but also relevant to Commission comments from ¶ 38 (II. A. Scope of Commission's Regulations) and ¶ 146 (II. B. 2. d. Pricing of Interconnection, Collocation, and Unbundled Network Elements).

[8] *NPRM* at ¶¶ 159-65.

[9] 47 U.S.C.A. § 410(c). *See also* In the Matter of Part 67 of the Commission's Rules and Establishment of a Joint Board, *Order*, CC Docket No. 80-286, 78 F.C.C. 2d 837 (1980).

access charge rules to recognize these new local arrangements in a forthcoming access reform proceeding.[10]

Second, an examination of the legislative history and sections 251(g) and (i) makes clear that section 251 was not designed to allow IXCs to circumvent the current tariff-based system of interstate access charges. The legislative history for the Senate bill version of section 251 of the Act provides:

> The obligations and procedures prescribed in this section *do not apply* to interconnection arrangements between local exchange carriers and telecommunications carriers under Section 201 of the Communications Act *for the purpose of providing interexchange service, and nothing in this section is intended to affect the Commission's access charge rules* [emphasis added].[11]

In addition, section 251(g) states that equal access and nondiscriminatory interconnection provisions that were effective prior to the Act's enactment on February 8, 1996 remain in place between incumbent LECs and IXCs "until such restrictions and obligations are explicitly superseded by regulations prescribed by the Commission after such date of enactment."[12] The Joint Explanatory

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[10] In the interim and prior to the advent of the access reform proceeding, waivers like the one NECA filed (*see* National Exchange Carrier Association, Inc. Petition for Waiver of Sections 69.104, 69.105 and 69.203 of the Commission's Rules for NECA Pool Members to Provide Unbundled Local Loops, CCB Pol. 96-06, filed Feb. 2, 1996) should be granted so that in areas where local competition is being initiated, the incumbent LECs can recover their costs of providing interstate access service. The Commission, in fact, granted similar waivers to Rochester Telephone Corporation prior to the adoption of the 1996 Act to allow it to recover the Subscriber Line Charge from carriers that purchase and resell its subscribers line as well as to recover the Carrier Common Line charges (CCL) from competing local service providers that purchase its subscriber lines, but not its local switching services. *See* Rochester Telephone Corporation Petition for Waivers to Implement Its Open Market Plan, *Order*, FCC 95-96, 10 F.C.C. Rcd 6776 (1995).

[11] *Joint Explanatory Statement* at 117. This Senate bill version was incorporated into the final 1996 Act.

[12] Section 251(g) of 1996 Act. Similarly, nothing in the Act supersedes existing joint provisioning arrangements between non-competing incumbent LECs and the Commission should not take any action that would restrict the use of these arrangements.

Statement states that this section was included to ensure that "equal access and nondiscrimination restrictions and obligations, *including receipt of compensation*," stay in place until the Commission deems it necessary to promulgate new regulations.[13]

Finally, to remove any further doubt, Congress put in a savings provision at section 251(i) which states that nothing in the Act is meant to limit or affect the Commission's authority under section 201. The current access charge system was adopted pursuant to section 201.

Neither the House Amendment nor the Conference Agreement reflect any comments contradicting the legislative history, or sections 251(g) or (i). Thus, the access charge rules remain fully effective and should not be changed in this local interconnection proceeding. Because the Act does not supersede the access charge regime, the Commission should not permit IXCs to purchase unbundled network elements in order to circumvent the existing access charge system. The correct course of action would be to keep the jurisdictional lines between intrastate and interstate access service distinct; to determine the local interconnection requirements within the specific time constraints set forth by the Act; and to ensure policies adopted in this proceeding are carefully coordinated with the pending universal service proceeding and any future access reform proceeding to avoid conflict of rules.

The Commission has recognized the need for review of the interstate access charge rules and NECA urges the Commission to initiate such a proceeding soon and recognize the interdependencies with the universal service proceeding, including the resolution of attendant subsidy issues.[14] Access

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[13] *See Joint Explanatory Statement* at 123 (emphasis added). Although the legislative history discusses the need for this section because the AT&T and GTE Consent Decrees are nullified by the Act, the statute itself states that all local exchange carriers are covered under this provision.

[14] *See NPRM* at ¶¶ 146, 165.

reform must be coordinated with the universal service and interconnection proceedings and is critical to accommodate and complement activity in the local arenas.

III. PRICING GUIDELINES SHOULD NOT SPECIFY DETAILED RATE STRUCTURES AND INCUMBENT LECS SHOULD BE ALLOWED TO RECOVER THEIR EMBEDDED COSTS[15]

The Commission states that "sections 251 and 252 do not make jurisdictional distinctions between interstate and intrastate services and facilities," and tentatively concludes that its pricing principles "would not recognize any jurisdictional distinctions, but would be based on some measure of unseparated costs."[16] As previously stated, such policy guidelines cannot change jurisdictional separations without the input of a Joint Board proceeding.[17] To the extent that the Commission can legally prescribe costing or pricing rules, these rules should (1) not specify any detailed rate structures and (2) permit LECs to recover their full embedded costs which were incurred under their obligation as carriers of last resort.

The Commission seeks comment on principles for analyzing rate structure questions, and some possible principles to guide state decisions in structuring rates for interconnection and unbundled network elements.[18] It further discusses and seeks comment on a number of specific rate structures schemes.[19]

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[15] This section addresses *NPRM* section II. B. 2. d. Interconnection, Collocation, and Unbundled Network Elements.

[16] *NPRM* at ¶ 120; *see also* ¶ 38.

[17] *See* discussion *supra*, at 3-4.

[18] *NPRM* at ¶ 149. These comments pertain to *NPRM* at section II. B. 2. d. (4).

[19] *Id.* at ¶¶ 150-54.

Since the intent of the 1996 Act is to encourage negotiations between parties,[20] the Commission should not specify detailed rate structure and pricing regulations at the local level to initiate local competition. Instead, broader, more flexible rules would allow telephone companies to recognize the differences in serving different classes of customers, different geographical areas, different density areas, individual customer requirements, and differences in underlying technology. Such broad guidelines would support use of negotiations as contemplated in the Act.

The Commission tentatively concludes that the states are precluded "from setting rates by use of traditional cost-of-service regulation, with its detailed examination of historical carrier costs and rate bases."[21] It adds "[i]nstead, the statute appears to contemplate the use of other forms of cost-based price regulation, such as price cap regulation that is indirectly based on costs, or the setting of prices based on a forward-looking cost methodology that does not involve the use of an embedded rate base, such as long-run incremental cost (LRIC)."[22] The Commission points out that it once defined LRIC as including "the full amount of incremental investment and expenses [incurred by] furnishing additional quantities of service, whether in a new or an existing service category," and added that, in estimating LRIC, one "determine[s] prospectively the effect on total costs, including the effect on common costs . . of adding units of service."[23] The Commission asked if this was still an appropriate definition and asked for a comparison with "Total Service" LRIC (TSLRIC).[24]

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[20] Section 252 of the 1996 Act anticipates negotiations based on the obligations set forth in section 251.

[21] *NPRM* at ¶ 123.

[22] *Id.*

[23] *Id.* at ¶ 126.

[24] *Id.* at ¶ 126. The Commission does not define or explain TSLRIC.

NECA agrees with the Commission's definition as well as its previous comments elaborating on the concept of LRIC -- as the Commission has stated, LRIC is basically a planning concept used to decide what combination of resources best suits projected demand.[25] "[A]ll inputs are variable, and all combinations of . . . factors of production are within [the planner's] grasp."[26] Common facilities will exist but are part of the overall investment decision.[27] If projected revenue covers projected costs, the firm will invest, otherwise it will not.

LRIC and total service LRIC (TSLRIC) are not useful principles for setting prices for jointly provided services. LRIC suffers from a series of flaws, most of which are also applicable to TSLRIC. Even the Commission has acknowledged that it "recognizes infirmities in [LRIC] and finds any strict translation of its procedures from theory to the practical telecommunications world infeasible."[28] NECA agrees with the Commission's recent examples of the difficulties raised by LRIC:

> First, attempting to determine the LRIC of a specific service for a particular LEC is likely to raise significant practical and administrative problems. [Second], given that services are provided over shared facilities and there are economies of scale and scope, setting the price of each discrete service based on [LRIC] will not recover the total costs of the network. [Third], where technological developments are reducing the costs of providing service, setting the price of discrete services equal to the forward-looking LRIC of each service is not likely to recover the historical, embedded costs of the network . . .[29]

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[25] American Telephone & Telegraph Co., Long Lines Dept., Revisions of Tariff FCC No. 260 Private Line Services, Series 5000 (TELPAK), *Memorandum Opinion and Order*, Docket No. 18128, 61 F.C.C. 2d 587 at 625 (1976).

[26] *Id.*

[27] *Id.*

[28] *Id.* at 626.

[29] Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, *Notice of Proposed Rulemaking*, CC Docket No. 95-185, FCC 95-505, at ¶ 48 (rel. Jan. 11, 1996).

Alternatively, the Commission should use a methodology that permits LECs, especially rural incumbent LECs, to recover their full embedded costs. Because all rate-of-return (ROR) companies' embedded costs are included in their rate bases, preventing these companies from recovering these costs in any new rate structure or pricing guidelines would be unduly economically burdensome. Nothing in the 1996 Act precludes cost-based regulation that would allow for recovery of embedded costs for determining the prices and rate structure of local interconnection.[30]

The Commission should also include a transition period or other cost-recovery mechanism in implementing any such new rules. If Commission pricing principles are imposed without a transition period or other recovery mechanism, subscriber costs would increase significantly (due to local rate increases from removal of support and rate rebalancing) in violation of the universal service principles of the 1996 Act.

The Commission must also recognize that incumbent LECs historically have been required to recover substantial plant investments using artificially long depreciation schedules. The introduction of competition in high cost areas, as contemplated by the 1996 Act, will materially alter capital recovery programs required under regulatory environments. Incumbent LECs have invested substantial amounts in plant to provide sufficient capacity to be "ready to serve" *all* of their customers. The costs of this additional capacity are not diminished by competition taking some customers from the incumbent. While depreciation schedules for rural incumbent LECs are primarily determined at the state level, failure to take account of these effects could result in stranded investment and ultimately jeopardize universal service. Local interconnection pricing requirements

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[30] The 1996 Act reference in section 252(d)(1) to rate of return is describing a type of regulatory proceeding rather than a pricing methodology. This section states that just and reasonable rates for interconnection of facilities shall be based on cost without a "rate-of-return or other rate-based proceeding."

that do not provide adequate transition mechanisms and other means of assuring cost recovery for incumbent LECs could jeopardize the rural incumbent LECs' ability to fully recover its embedded costs.[31]

It is critically important that pricing levels under any new system be based on the most accurate and complete cost of service information available. For rural incumbent LECs, actual cost data are the only proven, reliable basis for determining sufficient cost recovery levels.[32]

IV. CAREFUL CONSIDERATION SHOULD BE GIVEN TO RULE IMPACTS ON RURAL INCUMBENT LECS[33]

Interconnection rules developed with the larger companies in mind, but applied "across the board," can have unintentional, negative impacts on smaller rural companies with vastly different cost and service structures, and minimal or no competition.[34] Rural consumers should not have to bear

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[31] There must be a one-time transition to allow the incumbent LEC to recover these expenses. This is similar to the need that was recognized for the removal of CPE and inside wire from regulated accounts. *See* Procedures for Implementing the Detariffing of Customer Premises Equipment, CC Docket No. 81-893, *Report & Order*, 95 F.C.C. 2d 1276 (1983); Amendment of Part 31, Uniform System of Accounts for Class A and B Telephone Companies, CC Docket No. 79-105, *First Report and Order*, 85 F.C.C. 2d 818 (1981).

[32] An example of the need for special consideration for rural incumbent LECs is found in the universal service proceeding discussion of proxies. Several commenters in that proceeding support use of various proxy methodologies to determine costs. *See* NECA Reply Comments, *USF NPRM*, at 9-10, notes 21-23 (filed May 7, 1996). However, even those commenters recognize that proxy methods require additional study and improvement, and do not work well for rural incumbent LECs. *Id.* Therefore the Commission should not use a proxy or other cost surrogate for deriving rate principles that would adversely affect rural incumbent LECs.

[33] These comments address *NPRM* section II. F. Exemptions, Suspensions, and Modifications.

[34] Small rural telephone companies have fewer subscribers and serve larger geographic areas than their urban counterparts. *Telecommunications: America's Vital Link*, Access and Technology Planning Group, NECA, at 2 (1995). These companies also have dramatically higher costs of

any unreasonable costs associated with opening the local market to competition -- such a result would be contrary to the goals of universal service. Therefore, as the Commission proceeds, it should continually consider what impacts its proposed local competition rules will have on rural incumbent LECs.

Rural incumbent LECS have different market and operating constraints than larger incumbents. For example:

- Small size. Each employee of a rural incumbent LEC must perform multiple tasks and has little additional time for new administrative or regulatory requirements. More than half of NECA TS member companies operate with 10 or less employees.[35]

- Large operating territories. Large territories necessitate extensive investment in plant to provide service to all customers regardless of their location. Fifty-nine percent of the NECA TS member companies have service territories with over 200 square miles.[36]

- Small markets More than half of the NECA TS member companies have less than 20 customers per square mile, so unit costs per switch and per cable are higher than more urban areas.[37]

Faced with large service territories and few customers, it is no wonder that there are still 1,400 plus switches serving over 750,000 access lines which still do not have IXC competition via equal access.[38] The demand for local service competition is expected to be less than for equal

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providing local service because of the increased equipment costs deployed over sparsely populated areas. *Id.*

[35] *Id.* at 21.

[36] *Id.* at 11.

[37] *Id.* at 12.

[38] *See id.* at 26.

access.[39]

An example of an NPRM issue where the Commission must carefully consider impacts on rural incumbent LECs is determining whether it should set standards to assist the states regarding rural telephone company exemptions, suspensions and modifications.[40] Specifically, the Commission asks whether it should establish standards regarding what would constitute a "bona fide" request.[41]

Imposing local interconnection obligations on a rural incumbent LEC would not be in the public interest absent a need to incur the attendant costs. Thus, for example, any guidelines or rules regarding *bona fide* requests for collocation should be based on a viable method to allow LECs, especially rural incumbent LECs, to fully recover their costs. A *bona fide* request should include enough detailed information and specify adequate time frames to preclude any needless investment on the rural incumbent LEC's part.[42]

V. CONCLUSION

As stated in these comments, and recognized by the Commission, the purpose of this proceeding is to implement the provisions of the 1996 Act which require interconnection to open the

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[39] Approximately half of the respondents to NECA's survey do not believe competitors will enter their territory within the next three years. *Id.* at 13.

[40] *NPRM* at ¶ 261.

[41] *Id.*

[42] Consistent with section 251(f)(2) of the 1996 Act and the *Report and Order*, FCC Docket No. 78-72, Phase III (rel. March 19, 1985) dealing with equal access provisions, the Commission might consider establishing a reasonable interval from receipt of a *bona fide* request to implement the requested services. In addition, the Commission may wish to consider establishing *bona fide* request requirements for implementation of number portability for small incumbent LECs. For example, the Commission, in the case of equal access conversion, required non-Bell Operating Companies to convert to equal access within three years of receipt of a *bona fide* request.

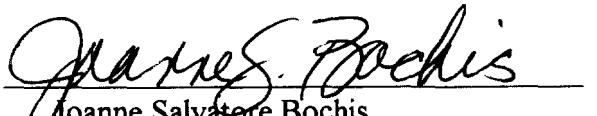
local telecommunications markets to competition. Nevertheless, this proceeding, the universal service proceeding, and an "upcoming proceeding to reform" the interstate access charge rules involve a tremendous number of overlapping, yet critical issues. NECA's comments highlight why the Commission must be wary to avoid promulgating conflicting rules in these different proceedings, or making them more complex than necessary.

NECA's comments show that the local interconnection provisions of the 1996 Act being implemented in this proceeding do not apply to interstate access or the provision of interexchange service. The 1996 Act does not provide any legal basis for permitting IXCs to avoid existing interstate access charge rules Rather, the rules or policies promulgated in this proceeding must recognize that current jurisdictional separations remain and that any changes to these procedures must be made via the Joint Board process.

NECA's comments also show that any local interconnection pricing guidelines adopted should not specify detailed rate structures, particularly where those rate structures would conflict with existing access charge rules; that LECs, especially rural incumbent LECs, should be permitted to fully recover their embedded costs which were incurred under their obligation as carriers of last resort; and that the Commission should carefully consider the effects of its rules on rural incumbent LECs.

Respectfully submitted,

NATIONAL EXCHANGE CARRIER ASSOCIATION, INC.

By: 

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May 16, 1996

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing Comments were served this 16th day of May, 1996, by hand delivery to the persons listed below.

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